Directorate of Intelligence

gross domestic product
foreign aid
deficit
savings
enterprise
unemployment
market
coal
energy
spending
exports
debt
taxes
consumption
investment
prices
equipment
industrialists
farms
imports
services
services
production
incentives
income
machine
decentralize
output
shortages
trade
trade
services
foreign aid
economy
statistics
capital investment
prices
stabilization
demand
living standards
inflation
natural gas
employment
goods
deficit
labor
layoffs
privatization
wages
controls
poverty
consumers
construction
real income

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Economic Survey of Russia

1992

Directorate of Intelligence

Economic Survey of Russia, 1992

This survey was prepared in the Economic Performance Division of the Office of Slavic and Eurasian Analysis, with a contribution from the Defense Programs Division.

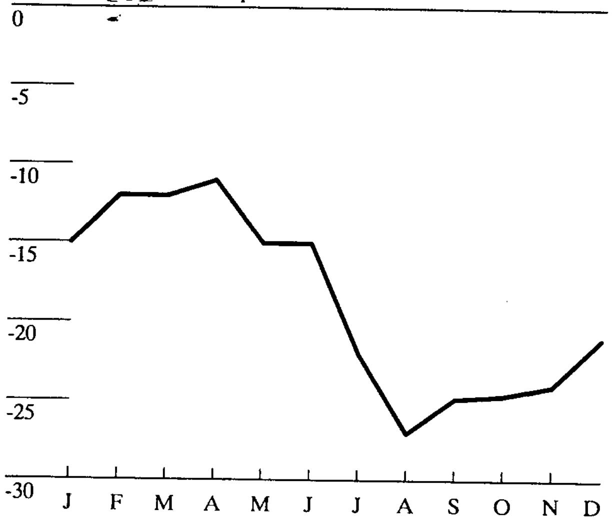
March 1993

Contents

Russian Economic Indicators, 1992

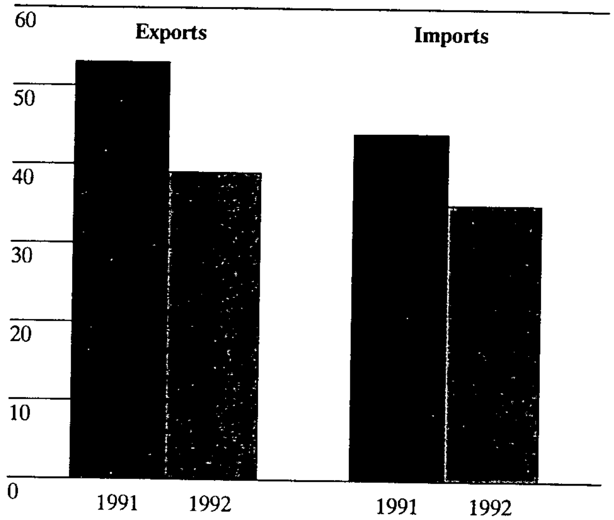
Industrial Output

Percent change over same period in 1991



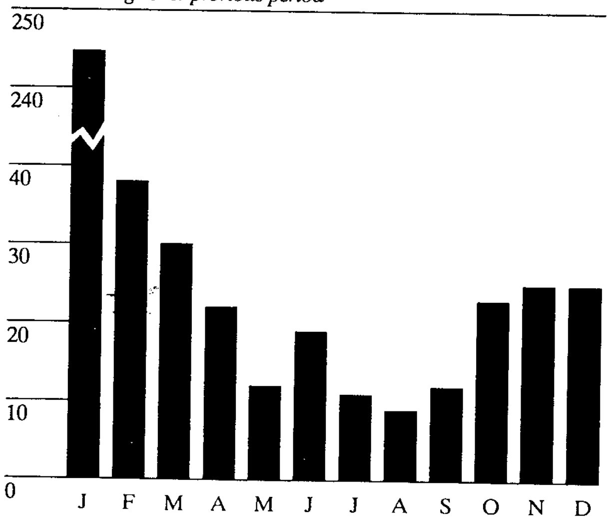
Foreign Trade

Billion US $



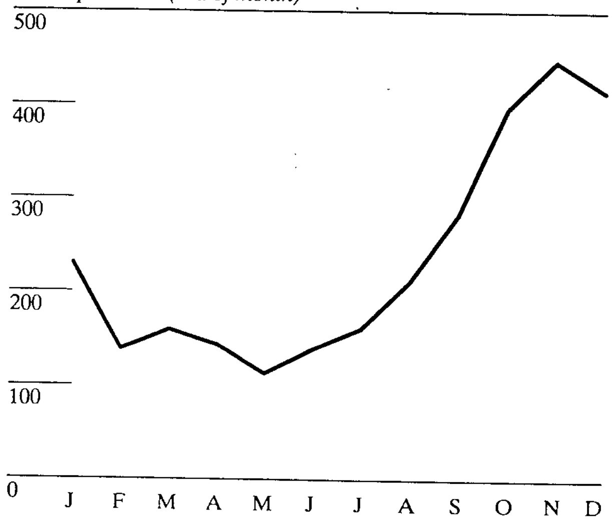
Retail Inflation

Percent change over previous period



Ruble Exchange Rate

Rubles per dollar (end of month)



Source: Russian official statistics.

Unclassified

338756 3-93

Summary of Key Developments

President Yel'tsin's government made significant strides toward a market economy in Russia last year by freeing most prices, cutting defense spending sharply, unifying foreign exchange rates, and launching an ambitious privatization program. At the same time, there was an across-the-board economic decline largely reflecting government efforts to restructure the economy, shortages of essential imports caused by the breakdown in former Bloc and interstate trade, and reduced demand following the freeing of prices in January.

Output Falls Sharply but Unemployment Remains Low. According to Russian official statistics, the output of all goods and services in 1992 fell for the third consecutive year, with industrial production declining by almost 19 percent and agricultural output by 5 percent. The actual decline, however, may have been less steep, because industrial and agricultural enterprises had strong incentives to understate output to avoid taxes, and official statistics may not have fully captured the output of the growing private sector. Despite the large drop in output, unemployment at yearend stood at an estimated 3 to 4 percent of Russia's 74-million-person labor force; many people, however, are working shortened weeks or are on forced leave.

Financial Stabilization Elusive. The resurgence of high inflation toward yearend largely reflected the price that Russia was willing to pay for maintaining high employment in the face of falling output. Moscow's financial stabilization program got off to a good start at the beginning of last year but began to falter by midyear. Through spring, the Russian leadership followed tight monetary and fiscal policies, enabling it to sharply reduce the budget deficit and the monthly rate of inflation. Under pressure from industrialists and the Supreme Soviet, the government loosened fiscal policies in the second half. In addition, the Russian Central Bank relaxed its tight credit policy in July at the behest of new Acting Chairman, Viktor Gerashchenko. This loosening of financial policies led to a sharp increase in prices during the last quarter, and inflation reached about 2,500 percent for the year.

The Plight of Most Consumers Worsens. Russia's January price liberalization and a blossoming of private vendors filled shelves across the country with previously scarce food items and consumer goods, but wages lagged inflation, making such goods unaffordable for many consumers. Falling real wages forced most Russians to spend a larger share of their income on food and to alter their eating habits. Indeed, many Russians reduced their consumption of higher priced meat, fish, milk, vegetables, and fruit, in favor of more bread and potatoes. As a result of higher spending on food, consumers reduced their consumption of nonfood goods and services.

Privatization Picks Up Steam. Despite a slow start and some rough going, the Russian Government by the end of 1992 scored some successes in its campaign to break the state's stranglehold on property and improve the environment for private businesses. More peasant farms were created than expected, the number of consumers purchasing goods from private traders rose sharply, the portion of the population working in the private sector increased to nearly one-fifth, and the nine-month-long slump in the privatization of small businesses was ended in the fall.

Defense Conversion Slow. Russia made little headway in restructuring the defense sector toward the production of consumer goods, but the number of defense plants attempting to do so increased markedly. Although the output of weapons fell sharply last year, most defense enterprises continued to encounter numerous difficulties developing and marketing new products, establishing new supply links, and securing resources for retooling. Moreover, total civil production by the defense sector fell in 1992 because of shortages of inputs and lower consumer demand caused by higher prices.

Bilateral Trade Plummets and Debt Remains a Problem. Ruptured ties with former trading partners, output declines, and sometimes erratic efforts to move to world prices and decentralize trade--foreign and interstate--took a heavy toll on Russia's commercial relations with other countries. For the second year in a row, foreign trade was down sharply, with exports falling by as much as 25 percent and imports by 21 percent. The drop in imports would have been much greater if foreign aid--worth an estimated $8 billion--had not allowed the continued flow of essential imports. Trade with the Eurasian States continued to decline, and support for the ruble as a common currency eroded in the face of loose monetary policies and rapidly rising prices throughout the region. At the same time, Russia paid only a fraction of the $20 billion due on the former USSR's roughly $80 billion debt; debt rescheduling remains hung up because of a dispute between Russia and Ukraine over division of the former USSR's assets. Capital flight also remained a serious problem in 1992.

Russian Output Indicators

Change in Real Output, 1991-92

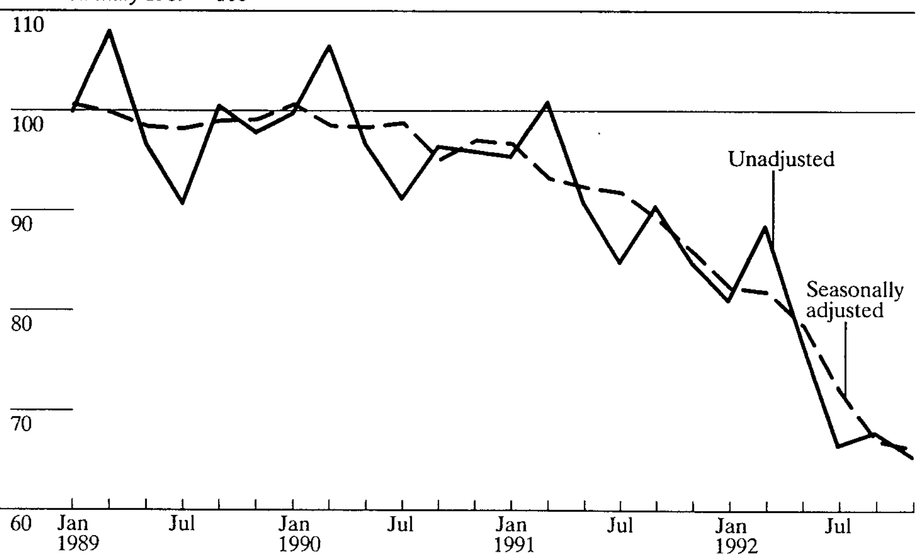
Percent change over same period of previous year

	1991	1992[b]	I	II	III	IV
GDP	-9	-19	NA	NA	NA	NA
National income produced	-11	-20	-14	-22	-24	-20
Industry	-8	-19	-13	-14	-26	-22
Oil	-10	-14	-13	-13	-16	-14
Gas	0.5	-0.4	0	0	-2	0.5
Coal	-11	-5	-1	3	-8	-8
Agriculture[a]	-8	-5	NA	NA	NA	NA
Grain	-24	20	NA	NA	NA	NA
Meat	-8	-11	NA	NA	NA	NA
Milk	-8	-10	NA	NA	NA	NA
Transportation						
Freight	-8	-22	-13	-19	-28	-28
Passenger	-5	-12	-11	-9	-16	-12

[a] Estimated, net of feed, seed, and waste.
[b] Preliminary.
Source: Russian official statistics, except for agriculture.

Industrial Production, 1989-92

Index: January 1989 = 100



Source: Russian official statistics, presented as a percent change over the same period of the previous year, have been adjusted to show month over month trends.

Unclassified

338757 3-93

Output Falls and Unemployment Rises

The Russian economy in 1992 contracted for the third consecutive year, with gross domestic product (GDP) falling by 19 percent, according to Russian official statistics. As a result, GDP was only about two-thirds of the 1989 level.

Production Down. Industrial output dropped almost 19 percent in 1992, more than double the decline recorded in 1991, according to Russian official statistics. Although the slump in output was across the board, the machinery and equipment sectors were particularly hard hit because of the 70-percent reduction in military procurement and the 45-percent cut in capital investment. In the energy sector, oil output declined 14 percent, coal was down 5 percent, and natural gas was virtually unchanged from 1991 levels. Production of consumer goods was 15 percent lower than in 1991.

Overall agricultural output fell roughly 5 percent from the depressed 1991 level, according to our calculations, although the production of most crops was up last year. The drop largely reflected the continued decline in the production of meat, milk, and eggs brought about by shrinking livestock herds and the increasing costs of inputs that made some output unprofitable; meat and milk output fell last year to their lowest levels in nearly a decade. Russia harvested 107 million tons of grain--clean weight--in 1992, about 20 percent more than in 1991. Meanwhile, the decline in state production of potatoes and other vegetables was largely offset by increased output from private plots and urban gardens. The private sector, for example, accounted for some 80 percent of potato production.

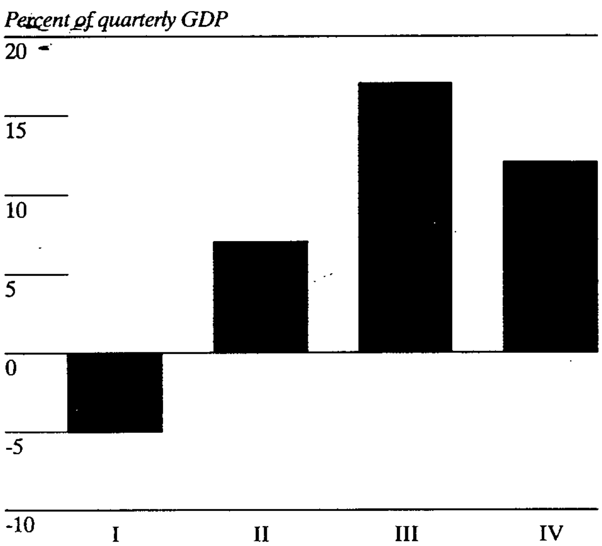
The production declines probably were not quite as bad as official statistics indicate. The drop in output may have been less steep, because enterprises had strong incentives to understate output to avoid taxes and keep goods for side deals. Moreover, official Russian data probably failed to fully capture the contribution of the country's growing private sector. In many cases, the fall in output was actually a good sign; besides reflecting a reduction in military production, many goods had been produced in excessive quantities. Indeed, price liberalization revealed the structural distortions that have accumulated over the years; the tremendous resource intensiveness of many sectors; and the poor quality, unprofitablility, or even negative value added at many industrial and agricultural enterprises.

Investment Slashed. Investment spending was cut by almost half last year as part of the government effort to reduce the budget deficit. Government hopes that other sources of investment--mainly enterprise funds--would help offset cuts in state funding were not fulfilled. Many enterprises were financially strapped and had little money to spend on capital improvements or repair. Moreover, as Russian officials noted, private savings were insufficient, investment institutions poorly developed, and foreign investment low because of the country's political and economic uncertainties. The cut in investment spending took a particularly heavy toll on energy, machine building, agroindustry, and construction. Uncompleted investment projects continued to proliferate, adding to inflationary pressures.

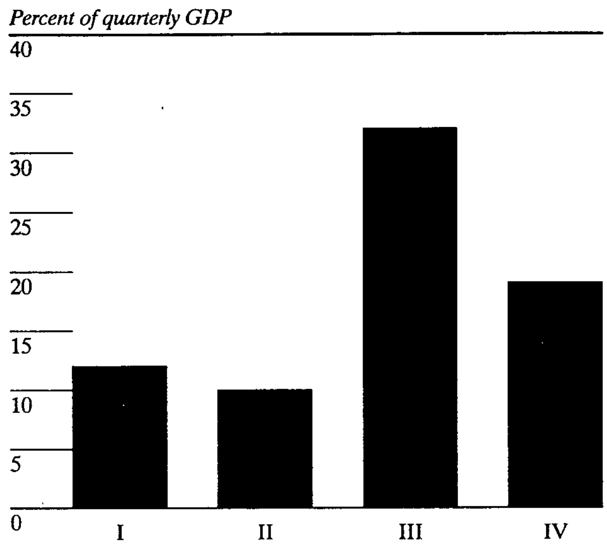
Unemployment Climbs. Despite the large drop in output, unemployment remained relatively low in 1992. Using a Western definition of unemployment, by yearend the jobless rate had climbed to about 3 to 4 percent of Russia's 74-million-person labor force. Unemployment would have risen more sharply if enterprises and the government had not taken measures to limit its growth. Many enterprise managers placed workers on shortened workweeks or extended leave with pay, and most dipped heavily into working capital and investment funds to pay wages. Indeed, the high priority that enterprise managers assigned to keeping their workforces intact partially explains the ballooning of interenterprise debt last year. For its part, the government began easing tight credit and spending policies at midyear--a move that helped unprofitable firms to pay their workers. Central bank credits, in particular, were targeted at large industrial firms, in part, to ward off massive layoffs.

Russian Financial Indicators, 1992

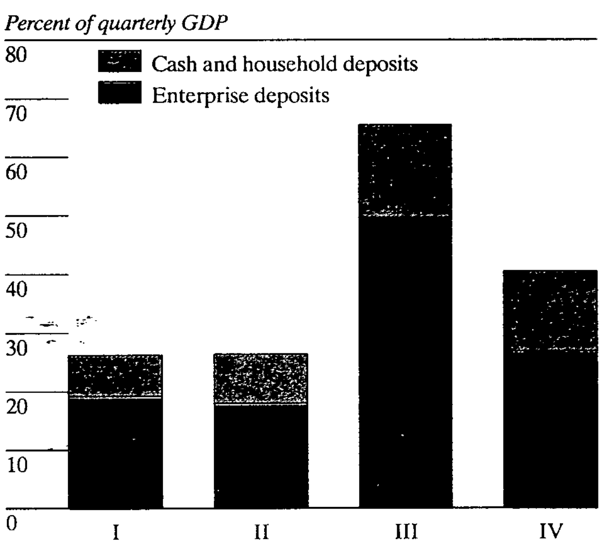
An Increasing Budget Deficit . . .



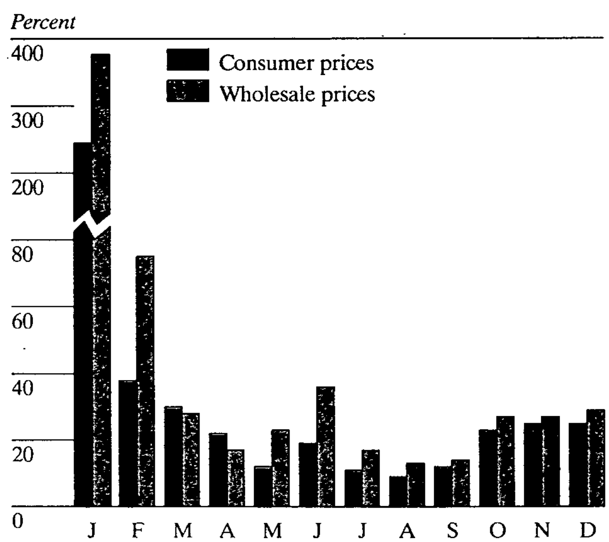
. . . and a Rise in State Credits . . .



. . . Resulted in a Sharp Increase in Money Supply . . .



. . . and Higher Monthly Inflation.



Source: Russian official data and CIA estimates.

Unclassified

338758 3-93

Financial Stability Erodes

When the Yel'tsin-Gaydar government took over in 1991, it inherited an economy that was in severe imbalance:

The budget deficit had reached approximately 20 percent of GNP, with the gap largely covered by the printing of money.

Despite administrative controls, prices were rising at an accelerating rate caused by the rapid growth of the money supply and the sharp drop in output.

Shortages of basic goods and food were rife.

Early Success. The government moved quickly to stabilize the financial situation by freeing most prices in January, cutting spending--particularly defense procurement and budget-funded investment--and overhauling the tax system. Besides helping to bring the demand for goods in line with supply, price decontrol allowed the government to reduce subsidies on food and other products. Meanwhile, tax reform, including the introduction of a new value-added tax, helped boost and stabilize government revenues despite implementation and collection problems.

The government's actions resulted in a sharp reduction in the budget deficit in the first half of the year and a steady decline in the monthly rate of retail price increases following the freeing of prices in January. By summer, the monthly rise in consumer prices had slowed to 10 percent. The inflation rate would have been even lower if the government had been able to restrict the growth of interenterprise debt. This debt climbed from 40 billion rubles at the end of 1991 to over 3 trillion rubles by 1 July.

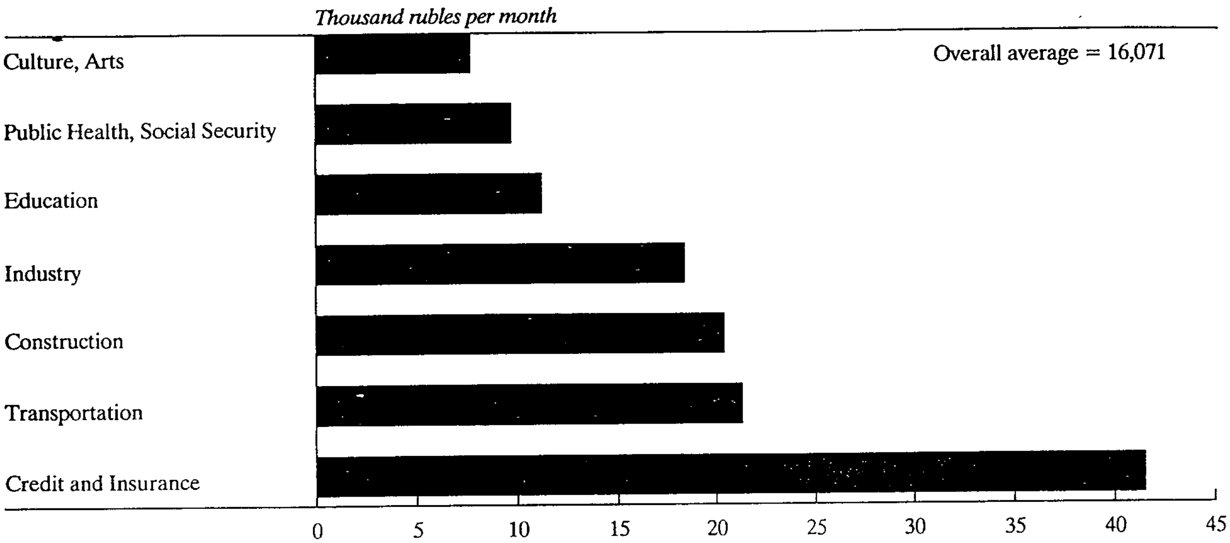
Stability Slips Away. Under pressure from industrialists, regional leaders, and the Supreme Soviet, the government loosened fiscal policy last summer to help financially strapped enterprises, ensure collection of the fall harvest, raise pensions and budget-funded wages, and provide for essential imports. The Russian Central Bank, meanwhile, relaxed its tight credit policy in July to ease the buildup of interenterprise debts and to increase working capital at the urging of its Acting Chairman Gerashchenko.

By September, the monthly inflation rate began to climb, compelling the government to try to tighten fiscal policy by sequestering expenditures. The government succeeded in running large budget surpluses in September and October by delaying state expenditures for investment and other uses. Success was short lived, however, because the budget apparently ran large deficits in November and December. Meanwhile, Central Bank credits to the economy and Eurasian states continued at a high level, and interenterprise debt reemerged despite rules designed to force enterprises to prepay for their purchases. During the fall, the overall money supply increased by an average of about 22 percent per month, roughly twice as fast as earlier in the year. As a result, monthly retail inflation rates hit about 25 percent per month during the fourth quarter. This contributed to the dramatic decline in the exchange rate of the ruble, which depreciated sharply against the dollar from July through December.

The failure of the government's monetary and fiscal policies to stem the decline in output contributed to Yel'tsin's replacement of Acting Premier Gaydar in December. His successor, Viktor Chernomyrdin, was viewed by many legislators as a pragmatic industrialist who would focus first on raising output and living standards. Chernomyrdin, however, has publicly said that achieving financial stability and reducing inflation are the most important immediate tasks.

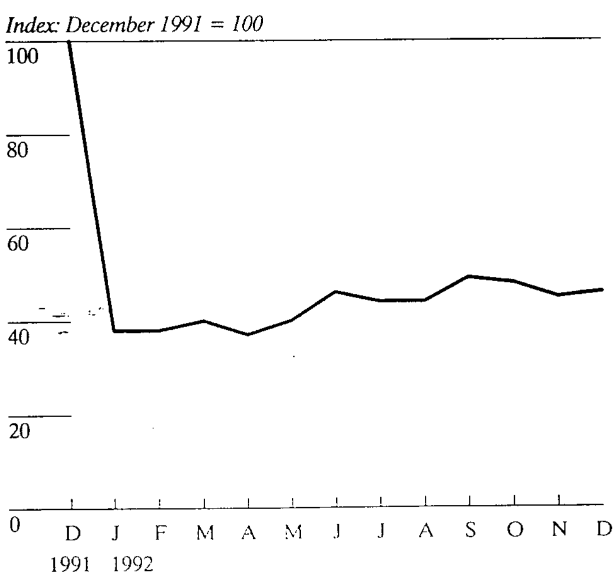
Russian Consumer Welfare Indicators, 1992

Average Wage by Sector, December 1992[a]

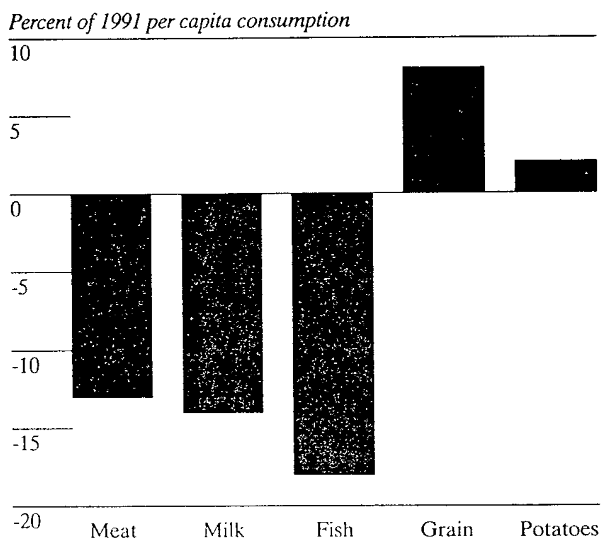


[a] Includes yearend bonus.

Real Average Wage



Shifting Consumption Patterns



Source: Russian official statistics.

Unclassified

338759 3-93

Living Standards Drop

Russia's January 1992 price liberalization filled store shelves across the country with previously scarce food products and other consumer goods, but wages lagged inflation, making such goods unaffordable for many Russians.

Prices Rise and Real Wages Fall. Consumer prices increased by roughly 2,500 percent in 1992, but wages grew by only about 1,400 percent, according to Russian official statistics. Living standards fell the most in January, when following liberalization, prices jumped 245 percent while wages grew by only 31 percent. The gap narrowed somewhat by yearend, but average per capita real income for the year was still about one-third lower than in 1991. The real income of pensioners, low-income families, and workers in budget-funded government, education, and health care jobs fell the most. The minimum pension was raised twice in 1992 but failed to keep up with the Russian Government's calculated minimum subsistence budget. By December, about one-third of the population reportedly earned less than 4,000 rubles per month, the official "poverty line."

The gap between the rich and poor widened, offending many Russians' ingrained sense of equity. In 1991, the incomes of the top 10 percent of the population were five times higher than the poorest 10 percent; by yearend 1992, it was roughly nine times greater. The increase in the disparity between the lower and upper income brackets reflects both the slow growth in pensioners' incomes and the high earnings of persons working in the emerging private sector. The gulf in average pay among the middle-income brackets also widened last year; the average pay of public health and education employees--who account for the bulk of budget-funded employees--and industrial workers grew by about two-thirds in 1992.

Consumption Down. Falling real income reduced total consumption and forced most Russians to spend a much larger share of their income on food. The average family spent about 45 percent of its income on food in 1992, as compared with 35 percent in 1991. Pensioners, meanwhile, reportedly spent over 80 percent of their incomes on food by yearend 1992, up 15 percentage points from 1991. The drop in real income also forced many Russians to alter their diet by reducing consumption of higher priced meat, fish, milk, vegetables, and fruit, in favor of more bread and potatoes. As a result, per capita consumption of milk fell by 14 percent, meat by 13 percent, and fish by 18 percent. In contrast, consumption of grain rose by 8 percent and potatoes by 2 percent. To help cope with the drop in real income, almost half of all Russian families now grow food at weekend homes and garden plots, according to a recent poll by the All-Russian Center for the Study of Public Opinion (VTsIOM).

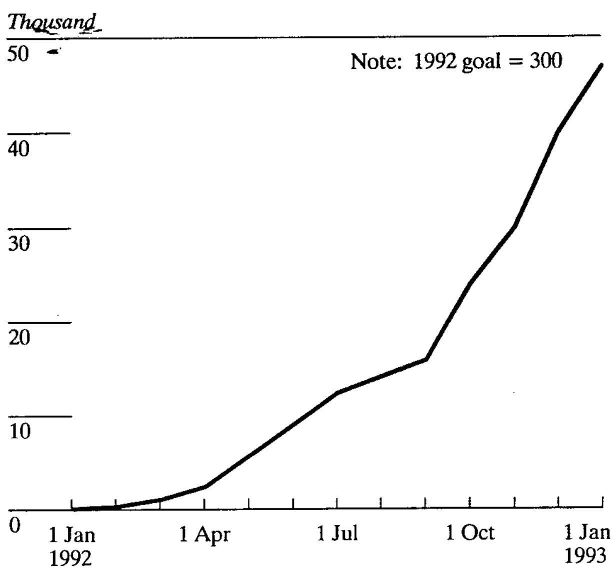
Higher spending on food contributed to reduced purchases of other consumer goods and services. For example, sales of knitwear, sewn goods, hosiery, and cotton fabrics fell by over 50 percent, and sales of shoes, woolens, and silks fell by over 25 percent. Consumers now plan to buy only essentials--shoes, coats, and clothing--and forego purchases of furniture, appliances, and cars, according to the VTsIOM poll. Russians also spent 36 percent less on services last year.

Food Availability Improves. Under price liberalization, scarce foods became available in stores and in farm markets throughout the country. Weekly government surveys showed that many basic foods--milk, beef, potatoes, onions, carrots, and cabbage--although high priced, were available in almost all of the 132 cities surveyed during most of the year. Farm markets also were well stocked, but prices were substantially higher. The weekly surveys, however, found shortages of pork, canned fish, rye bread, and some types of noodles in about half of the surveyed cities, particularly during the winter. Local price controls and high transport costs led to food shortages and rationing in some cities in the Urals, Siberia, the Far East, and the far north.

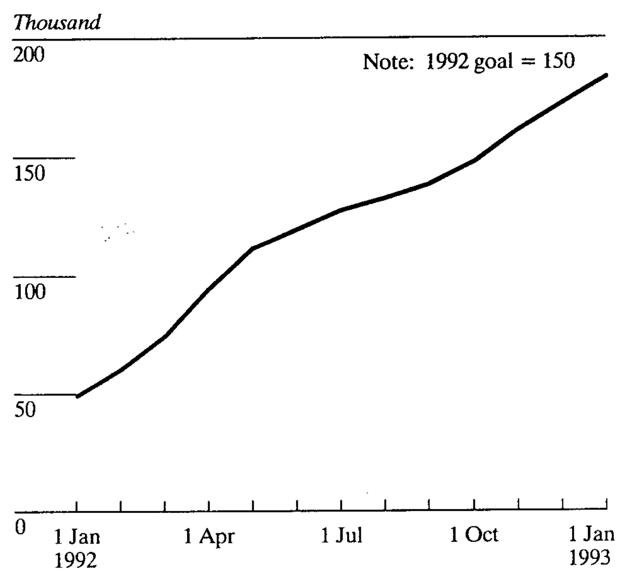
Housing Construction Declines. State and private construction of new housing was down almost a quarter in 1992, according to Russian official statistics. Most of the drop in the state sector--which accounted for 83 percent of total housing construction last year--stemmed from the cutback in government funding. The decline in the construction of private homes was caused by soaring costs that put such housing out of the reach of most Russians. Moreover, some citizens who could cover the exorbitant costs were stymied by shortages of building materials.

Russian Privatization Indicators, 1992

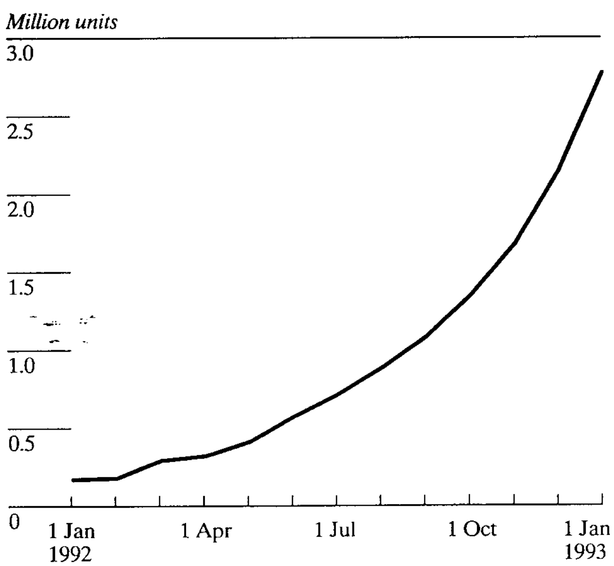
Small Businesses Privatized



Peasant Farms Created



Housing Privatized



Source: Russian official statistics and CIA estimates.

Unclassified

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Privatization Gains Momentum

The private sector assumed more importance in the Russian economy last year. According to official statistics, the volume of consumer goods purchased from private shops rose from a negligible amount in 1991 to more than 4 percent in 1992. Purchases from street traders who operated at open-air markets, street corners, and sidewalk kiosks were also up last year and accounted for 12 percent of total spending on consumer goods. Private-sector employment blossomed as well. Russian official data report that about 15 million people--approximately 20 percent of the labor force--were privately employed in 1992. In addition, one out of six Russians moonlighted in the private sector, and half of Russian families raised some of their own food.

Small Businesses Spotlighted. Yel'tsin, believing that it was necessary to create a large propertied class that would promote social stability and have a stake in economic reform, declared that "1992 would be the year of privatization." The government focused its efforts mainly on small businesses, delaying privatization of industry until 1993. Moscow reasoned that there would be little opposition to a change in ownership for small firms because they could be privatized quickly and consumers would benefit from the likely improvement in supplies. To this end, the government began a crash campaign to sell 60 percent of small shops, restaurants, and service establishments--largely through auctions. The selloff of small businesses was slow during most of the year, but picked up dramatically during the last quarter of 1992, when the government announced that citizens could use their 10,000-ruble privatization vouchers--which were distributed to all Russians beginning in October--to buy these properties. By yearend, 47,000 firms--more than double the number in October and about 13 to 15 percent of those scheduled for privatizing--had been sold. Privatization proceeded at a particularly fast pace in the proreform cities of St. Petersburg, Nizhniy Novgorod, Vladimir, Orel, and Belgorod, where progressive local leaders were able to create a consensus for change.

Despite the accelerated pace late in the year, the government fell short of its 1992 privatization target. Privatization czar Anatoliy Chubays blamed paperwork problems, but the more important causes were that most Russians lacked the investment capital to buy businesses and were reluctant to take the risks of ownership. To the government's disappointment, virtually no foreigners sank their money into the new companies.

Privatization of Farms and Housing Up. The program to turn agricultural land over to independent farmers accelerated in 1992. The number of private farms more than tripled, to 184,000, far exceeding the government's 1992 target. Despite the rapid growth, however, these private farms accounted for less than 4 percent of Russia's agricultural land and production. Moreover, private farmers continued to be dependent on the state for inputs, machinery, and credit. The Russian Government, meanwhile, managed to turn 2.6 million dwellings--out of a state stock of about 33 million units--over to citizens last year, the vast majority for free.

Defense Conversion Effort Finds Incentive

In 1992, progress on defense conversion was slow. Enterprise managers, however, began to take conversion seriously in response to the Russian government's cut in weapons orders by roughly 70 percent. Yel'tsin also signed a conversion law in March 1992 that offers guidelines for shifting to civil production, but its impact has been limited by the leadership's continued indecision over which weapon programs and plants it needs to retain. In addition, economic reforms--especially price liberalization and privatization--have begun to force firms to restructure themselves to produce goods that are in demand.

Defense Sector Production Plummets. Russian officials publicly claim that the production of weapon systems fell by 50 percent or more last year. Some plants ceased production entirely, while others continued to manufacture arms without orders or customers. Mounting inventories made plant managers desperate to find foreign buyers. Although many officials looked to arms sales abroad to keep plants active and to finance conversion, hard currency sales were down by half last year.

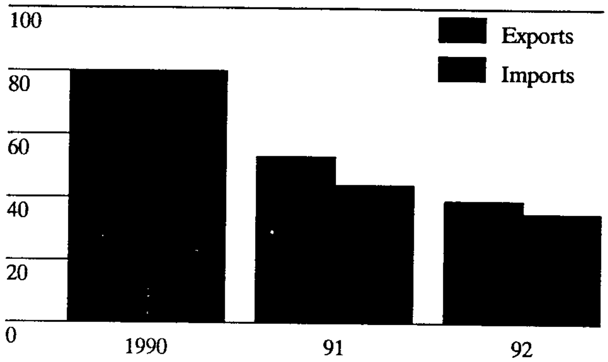
Civil production by the defense-industrial sector also fell in 1992 because of a shortage of materials and declining demand caused by price increases. According to Russian official statistics, production of televisions, refrigerators, and washing machines--almost all of which are made by defense plants--fell by 15 to 25 percent. Most enterprises continued to face problems developing and marketing new products, establishing new supply links, securing resources for retooling, and attracting foreign aid and investment.

Financial Problems Formidable. Many financially strapped defense plants managed to keep operating by running up interenterprise debts and by relying on Central Bank credits--many of which were on preferential terms. In addition, defense enterprises diverted most of the 150 billion rubles the government earmarked last year to finance conversion to meet payrolls. These actions averted large-scale unemployment among Russia's 5 to 8 million defense-industrial workers, although, according to Russian press, roughly 600,000 defense workers left the sector primarily for higher paying jobs in the civil sector. Underemployment, however, was widespread, with many thousands of workers on extended leave and, reportedly, more than 400 defense plants operating only three to four days a week. In addition, over 2 million industrial workers were only partially employed, and at least half of these probably were in the defense sector.

Defense Industrialists Split. While a small--but growing--number of defense plant officials welcomed their new freedom and endorsed the government's economic reforms, including privatization, the worsening situation drove many defense industry leaders to join with other industrialists and call for a slowdown in the pace of economic reform. These groups lobbied the government to channel additional credits to unprofitable enterprises, including defense plants, to hold down unemployment, even at the risk of hyperinflation.

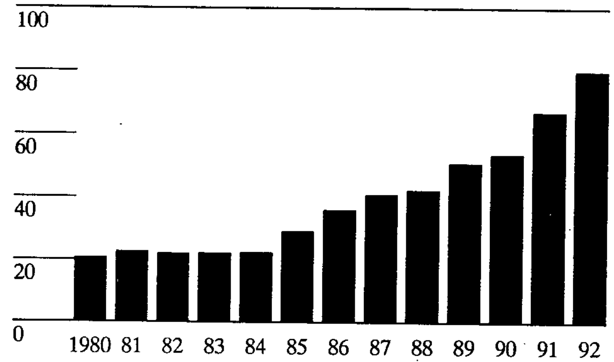
Russian Foreign Economic Indicators, 1992

Foreign Trade



Source: Goskomstat data. Excludes trade with former Soviet Republics and the Baltic States.

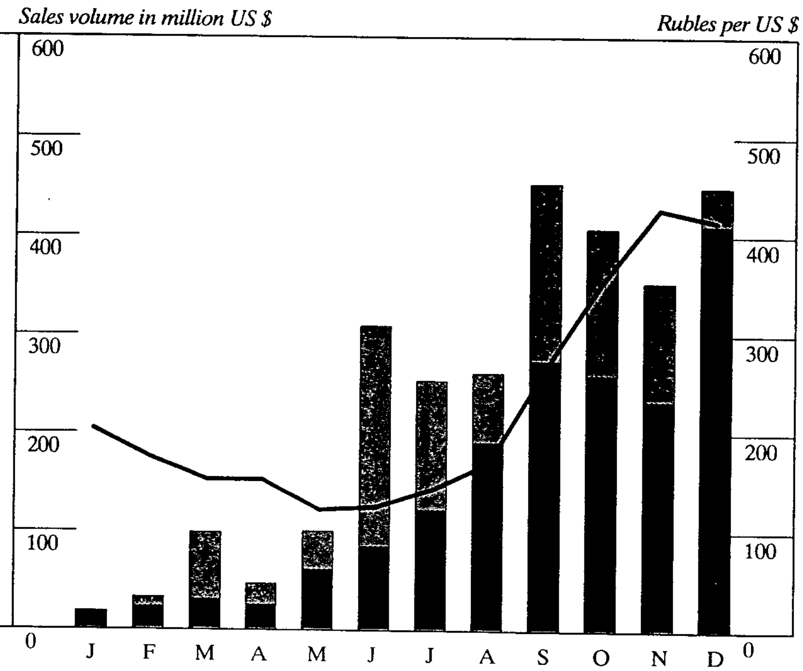
Estimated Hard Currency Debt of the States of the Former USSR, 1980-92



Source: CIA estimate.

The Ruble/Dollar Exchange Rate [a]

Monthly Sales Volume
- Sold by Central Bank [b]
- Sold by commercial enterprises to Central Bank [b]
- Sold by commercial enterprises to other enterprises



[a] Moscow Interbank Currency Exchange.

[b] Central Bank "intervention."

Source: Central Bank of Russia.

Unclassified

338761 3-93

Foreign Economic Relations Still in Turmoil

Russia's foreign trade in 1992 dropped sharply for the second year in a row. Moscow, meanwhile, made little headway on reaching a debt agreement with foreign creditors, and foreign investors remained cautious because of the country's political and economic uncertainties.

Foreign Trade Falls. Trade with countries other than the Eurasian states fell in 1992 by as much as 23 percent.[1] The decline primarily reflects falling Russian output, hard currency shortages, problems with transportation links through Eurasia, and difficulty financing trade with former CEMA partners. Russia's foreign trade regulations--hard currency surrender requirements, licensing rules, and tariffs--and Moscow's tendency to modify these rules with little advance notice also inhibited trade. A growing share of the country's foreign trade last year was conducted by Russian enterprises, and many skirted the government's trade rules by illegally exporting and importing various goods and by depositing as much as $8 billion in export earnings in foreign banks.

The composition of Russian foreign trade in 1992 mirrored past years, with Russia largely a seller of raw materials and a buyer of manufactured goods and food. Sales of oil and natural gas earned Russia around $20 billion, or almost half of all export earnings. Other commodities such as chemicals, metals, and timber also were significant export items, while manufactured goods--including arms--probably accounted for less than 20 percent of Russia's total sales. On the import side, machinery and equipment comprised about 40 percent of Russian purchases and food, and agricultural products make up more than 25 percent.

Shifts in the regional pattern of Russian foreign trade occurred as some partners were hit harder than others by the drop in Russia's trade. Trade with Developed Western countries, for example, fell less than trade with other regions because of the West's willingness to pay cash for Russia's exports and to provide credits for many of Russia's purchases. Exchanges with Moscow's former CEMA partners, meanwhile, were down sharply, reflecting financing troubles that forced most trade to take place on barter terms. And trade with most Third World regions plummeted; East Asia was the exception because of the strength of increased trade with China.

Hard Currency Debt Goes Unpaid. Russia was the only Eurasian state to make any payments in 1992 on the $20 billion due on the debts of the former USSR. Moscow, however, was able to pay only about $1.5 billion of its share of roughly $12 billion because of weak export performance, continued capital flight, and a lack of foreign investment. In late 1991, Russia and seven of the other Eurasian states accepted joint responsibility for the foreign debt and set up a mechanism to service their individual shares through the Vnesheconombank (VEB). This arrangement, however, quickly broke down because the non-Russian states did not have significant sources of hard currency and refused to channel their payments through the Russian-controlled VEB. Russia has since concluded agreements with all of the Eurasian states except Ukraine to assume responsibility for their share of the debt in return for their renunciation of a claim on assets of the former USSR.

Toward the end of last year, Russia began negotiations with the Paris Club on a comprehensive debt rescheduling but was unable to reach a quick agreement because of differences over the amount of debt service to be paid in 1993. Negotiations were also complicated by Ukraine's insistence on retaining responsibility for its share of the debt and servicing it independently of Russia in exchange for receiving a proportional share of the assets of the former USSR. At yearend, the hard currency debt of the Eurasian states totaled an estimated $80 billion.

Foreign Investors Still Wary. Foreign investment continued to play only a small role in Russia's economy in 1992, with inflows estimated at only a few hundred million dollars. Foreign investors were discouraged by Russia's lack of a sound legal system, the nonconvertability of the ruble, Moscow's inability to implement an IMF stabilization program, and the uncertain political climate.

[1] The State Statistical Committee, Goskomstat, reported that foreign trade fell by 23 percent in 1992. The Ministry for Foreign Economic Relations' figures show that foreign trade fell by 9 percent last year. The Goskomstat figures probably overstate the decline in foreign trade last year because of their failure to account for small enterprises and illegal activities. The Ministry's figures, however, probably understate the decline because they include some interrepublic trade.

Exchange Rate Falls as Inflation Rises. The ruble fell precipitously in value in 1992 because of high inflation and a flight to foreign assets. At midyear, the government unified the ruble rate by abolishing its administratively set official and special commercial rates, and began setting its new official rate on the basis of biweekly hard currency auctions in Moscow. Although the government intervened heavily at these auctions to support the ruble, loose monetary policies during the latter half of the year caused the ruble to fall to 415 rubles per dollar by yearend. As a result, at the end of December the ruble was worth about a third of what it had been at the start of 1992.

Ruble Zone Shrinks. In 1992, Russia's trade with other Eurasian states continued to decline, while support for the ruble as a common currency eroded in the face of loose monetary policies and rapidly rising prices within the ruble zone. The decline in ruble zone trade primarily reflected Moscow's efforts to move to world prices and decentralize trade coupled with production declines in the region. Moscow increased energy prices from 2,700 to 8,000 percent depending on each state's economic and political relationship with Russia. Because the other Eurasian states were unable to pay the higher costs, Moscow cut back sharply on deliveries of oil and other goods to limit its growing bilateral trade deficits. Moscow's decentralization of interstate trade also forced the other Eurasian states to negotiate directly with Russian enterprises to purchase goods previously acquired through state channels. Russian enterprises producing goods readily marketable in the West, however, were increasingly reluctant to sell their products for rubles. As a result, most of the Eurasian states resorted to barter to carry out essential transactions. Growing payment arrears brought about by an ineffective banking system also contributed to the fall in trade across the region.

Russia became increasingly concerned last year that the credit emissions and large trade deficits of other Eurasian states were undermining Moscow's reforms and spurring inflation in Russia. Some Russian officials demanded that the other states abide by Russia's monetary policies or leave the ruble zone. Moscow at midyear began refusing to process trade payment orders from other Eurasian states unless bilateral trade was in balance. It also cut back on credits to Eurasian states running trade deficits. Moscow eventually eased these policies because they severely crimped trade. Four states--Estonia, Latvia, Lithuania, and Ukraine--left the ruble zone and issued their own currencies in the second half of 1992, and other Eurasian states are contemplating similar moves.

Status of the Ruble Zone

OUT	
Estonia	The kroon national currency was issued in June 1992.
Latvia	The rublis coupon replaced the ruble in May 1992.
Lithuania	The talonas coupon replaced the ruble in October 1992.
Ukraine	The karbovanets coupon replaced the ruble in November 1992.
ALMOST OUT	
Azerbaijan	The manat has been circulating in parallel with the ruble since August 1992.
Turkmenistan	The government plans to issue a new currency later in 1993.
STILL IN	
Russia	A new ruble note is gradually replacing the old Soviet-style currency.
Belarus	The rubel coupon is being used in parallel with the ruble.
Moldova	The lei currency will be issued pending Russia's actions.
Georgia	The government has decided to leave the ruble zone, but no date has been set.
Kyrgyzstan	A national currency is being prepared for use later, but no date has been set.
Armenia	A national currency is being printed, but no date has been set for its release.
Kazakhstan	A national currency is being prepared, but the ruble is still in use.
Uzbekistan	Contingency plans for a new currency are under way, but the ruble is still used.
Tajikistan	The government is planning a parallel currency to be coordinated with the ruble.